

# *Office of the State Auditor*

## *Division of State Audit*

### Department of Commerce Bismarck, North Dakota

Audit Report for the  
Biennium Ended June 30, 2007  
Client Code 601

*Robert R. Peterson*  
*State Auditor*



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## *Transmittal Letter*

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August 21, 2007

The Honorable John Hoeven, Governor  
Members of the North Dakota Legislative Assembly  
Shane Goettle, Commissioner, Department of Commerce

We are pleased to submit this audit of the Department of Commerce for the biennium ended June 30, 2007. This audit resulted from the statutory responsibility of the State Auditor to audit or review each state agency once every two years. The same statute gives the State Auditor the responsibility to determine the contents of these audits.

In determining the contents of the audits of state agencies, the primary consideration was to determine how we could best serve the citizens of the state of North Dakota. Naturally we determined financial accountability should play an important part of these audits. Additionally, operational accountability is addressed whenever possible to increase efficiency and effectiveness of state government.

The in-charge auditor for this audit was Allison Bader. Paul Deede and Aaron Petrowitz were the staff auditors. Cindi Pedersen, CPA, was the audit supervisor and Ron Tolstad, Jr., CPA, was the audit manager. Inquiries or comments relating to this audit may be directed to the audit manager by calling (701) 328-2243. We wish to express our appreciation to Commissioner Shane Goettle and his staff for the courtesy, cooperation, and assistance they provided to us during this audit.

Respectfully submitted,

Robert R. Peterson  
State Auditor

# *Executive Summary*

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## **INTRODUCTION**

The North Dakota Department of Commerce has been in existence since July 2001 and was charged with the task of strengthening and streamlining the state's economic development efforts. Legislation authorized the merger of three former state agencies: Community Services; Economic Development and Finance; and Tourism. Additionally, the Workforce Development Division was created within the Department of Commerce.

## **RESPONSES TO LAFRC AUDIT QUESTIONS**

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The Legislative Audit and Fiscal Review Committee (LAFRC) requests that certain items be addressed by auditors performing audits of state agencies.

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### *1. What type of opinion was issued on the financial statements?*

Financial statements were not prepared by the Department of Commerce in accordance with generally accepted accounting standards so an opinion is not applicable. The agency's transactions were tested and included in the state's basic financial statements on which an unqualified opinion was issued.

### *2. Was there compliance with statutes, laws, rules, and regulations under which the agency was created and is functioning?*

Other than our finding addressing "noncompliance with procurement laws" (see page 18), the Department of Commerce was in compliance with significant statutes, laws, rules, and regulations under which it was created and is functioning.

### *3. Was internal control adequate and functioning effectively?*

Other than our finding addressing the "investment controls weakness" (see page 14) and "inventory controls weaknesses" (see page 15), we determined internal control was adequate.

### *4. Were there any indications of lack of efficiency in financial operations and management of the agency?*

Other than our work addressing "economic development grant improvements" (see page 20) there were no indications of lack of efficiency in financial operations and management of the Department of Commerce.

5. *Has action been taken on findings and recommendations included in prior audit reports?*

Other than the "inventory procedures control weakness" (see page 24), all recommendations included in the prior audit report were implemented.

6. *Was a management letter issued? If so, provide a summary below, including any recommendations and the management responses.*

Yes, a management letter was issued and is included on pages 25-26 of this report, along with management's response.

### **LAFRC AUDIT COMMUNICATIONS**

1. *Identify any significant changes in accounting policies, any management conflicts of interest, any contingent liabilities, or any significant unusual transactions.*

There were no significant changes in accounting policies, no management conflicts of interest were noted, no contingent liabilities were identified or significant unusual transactions.

2. *Identify any significant accounting estimates, the process used by management to formulate the accounting estimates, and the basis for the auditor's conclusions regarding the reasonableness of those estimates.*

The Department of Commerce's financial statements do not include any significant accounting estimates.

3. *Identify any significant audit adjustments.*

Significant audit adjustments were not necessary.

4. *Identify any disagreements with management, whether or not resolved to the auditor's satisfaction relating to a financial accounting, reporting, or auditing matter that could be significant to the financial statements.*

None.

5. *Identify any serious difficulties encountered in performing the audit.*

None.

6. *Identify any major issues discussed with management prior to retention.*

This is not applicable for audits conducted by the Office of the State Auditor.

7. *Identify any management consultations with other accountants about auditing and accounting matters.*

None.

8. *Identify any high-risk information technology systems critical to operations based on the auditor's overall assessment of the importance of the system to the agency and its mission, or whether any exceptions identified in the six audit report questions to be addressed by the auditors are directly related to the operations of an information technology system.*

ConnectND Finance, Human Resource Management System (HRMS), and HOMENet applications are high-risk information technology systems critical to the Department of Commerce.

## ***Background Information***

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**T**he Department of Commerce is the lead agency charged by the Governor and state Legislature with growing North Dakota and improving the quality of life for North Dakota people. The mission of the Department of Commerce is to attract, retain, and expand wealth.

The agency partners with local, state, federal, public, private, and non-profit organizations and is the primary facilitator for all entities statewide that are involved in the economic and community development process.

The work of the Department of Commerce is organized within four divisions: Community Services; Economic Development and Finance; Workforce Development; and Tourism. The Agency also works with the North Dakota Economic Development Foundation, which serves as a private-sector advisory board to the Governor and Department of Commerce.

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Dept of Commerce includes:

- Division of Community Services.
  - Economic Development and Finance.
  - Workforce Development.
  - Tourism Division.
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The Division of Community Service assists local governments and state agencies with community and rural development, policy research, and development and implementation of grant programs. The goal of Community Services is to provide effective, efficient, and customer-oriented administration of federal and state programs for community development, energy efficiency, housing and self-sufficiency. The Division of Community Services administers a variety of grant and regulatory programs including: the Community Development Block Grant; HOME; Emergency Shelter Grants; Renaissance Zone; State Building Code; Third-party Inspection; Manufactured Home Installation; Weatherization Assistance; Community Services Block Grant; State Energy; State Building Conservation; Self-Reliance; and Community Food and Nutrition programs.

The Economic Development and Finance Division (ED&F) provides strategic direction and services to stimulate and support local economic growth and diversity. The Division's primary goal is to increase the state's household and per capita income through its strategic planning, policy development, and service offerings. The Division operates a variety of programs aimed at strengthening North Dakota's business climate, increasing the state's global competitiveness, and accelerating job growth in the five target industries in order to retain the current workforce and attract new high-skilled labor. The Division's primary activities are state and local project development, research and intelligence, business and workforce development, and financial services including the Ag Products Utilization Commission, and the North Dakota Development Fund.



The Workforce Development Division serves as the state's change agent, convening agent, accountability agent, and champion for workforce and service issues. The Workforce Development Division is responsible for developing a statewide talent recruitment initiative and for providing administrative support for several state and federally mandated commissions. These include the North Dakota Workforce Development Council, the North Dakota Youth Development Council, and the State Commission on National and Community Service. The goals of the Division are ensuring that North Dakota employers have access to a skilled and available workforce, retaining young people and promoting the expansion of civic engagement and volunteerism in the state.

The Division of Tourism is working to create new wealth for North Dakota through increased spending by out-of-state visitors. To accomplish this mission, the Tourism Division operates seven program areas: tourism (leisure) marketing; international marketing; group travel; Lewis and Clark/cultural and heritage tourism (including learning-based vacations); outdoor promotions; and public/media relations. The Division provides marketing and promotional support to the state's tourism industry as a whole and to individual communities, events, and attractions. The Division serves travelers both in and out-of-state through the State Tourism web-site, mailings, a toll-free telephone number, and by distributing the state travel guide. State Tourism also works with national and international travel planners and media to promote travel to North Dakota. Tourism programs provide opportunities for North Dakota businesses to market themselves along with the state in a variety of ways including trade show participation, cooperative advertising, brochure distribution programs, marketing grants, web-site listings, and hosting media.

The North Dakota Economic Development Foundation is a private-sector advisory group charged with providing guidance to the Governor and the Department of Commerce on economic development issues. The Foundation includes 21 members, appointed by the Governor, representing a broad range of industries, higher education, and students statewide. In 2002, the Foundation developed a 10-year Strategic Plan for Economic Development in North Dakota. The plan includes specific goals and benchmarks for economic growth. The Foundation monitors progress toward these goals at quarterly meetings held throughout the state. The Foundation monitors tourism and economic development activities and initiatives of the Department of Commerce; recommends state and federal legislation relating to strengthening the state's economy and increasing the state's population; monitors state and federal legislation and initiatives that may impact the state's economy and population; and provides expertise for developing public and private initiatives to strengthen the state's economy and increase the state's population.

More information about the agency can be obtained from the Department of Commerce's home page at:

<http://www.ndcommerce.com/>.

The Agency regularly reports to the Legislative Commerce and Economic Development Committees in addition to the Budget Section.

# ***Audit Objectives, Scope, And Methodology***

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## *Audit Objectives*

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The objectives of this audit of the Department of Commerce for the biennium ended June 30, 2007 were to provide reliable, audited financial statements and to answer the following questions:

1. What are the most important areas of the Department of Commerce's operations and is internal control adequate in these areas?
2. What are the significant and high-risk areas of legislative intent applicable to the Department of Commerce and are they in compliance with these laws?
3. Are there areas of the Department of Commerce's operations where we can help to improve efficiency or effectiveness?

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## *Audit Scope*

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This audit of the Department of Commerce for the biennium ended June 30, 2007 was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. To meet the objectives outlined above, we:

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## *Audit Methodology*

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- Prepared financial statements from the legal balances on the state's accounting system tested as part of this audit and the audit of the state's Comprehensive Annual Financial Report and reviewed management's discussion and analysis of the financial statements.
- Performed detailed analytical procedures for expenditures and receipts.
- Tested samples of expenditures, journal vouchers, and correcting entries.
- Reviewed prior year audit workpapers.
- Interviewed appropriate agency personnel.
- Reviewed Department of Commerce written plans and applicable manuals.
- Observed Department of Commerce's processes and procedures.
- Reviewed North Dakota Century Code chapters 21-11 and 54-34.3.
- Reviewed 2005 Session Laws including the agency's appropriation.
- Reviewed industry best practices through the use of Internet searches.
- Reviewed the processes and procedures for the purchases, sales, give-aways, storage, and segregation of duties surrounding inventory available for sale.

- Reviewed the policies and procedures surrounding economic development grants.

## ***Discussion And Analysis***

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The accompanying financial statements have been prepared to present the Department of Commerce's revenues and expenditures on the legal (budget) basis. The accompanying financial statements are not intended to be presented in accordance with generally accepted accounting principles (GAAP).

For the biennium ended June 30, 2007, operations of the Department of Commerce were primarily supported by federal funds either received directly or passed-through from another state agency. This is supplemented by general funds and fees credited to the agency's operating fund.

### ***FINANCIAL SUMMARY***

Revenues and other sources consisted primarily of federal funds, as well as transfers and loan principle and interest revenue. Program income included revenue related to the innovate ND, manufactured home, labor availability study, and international business and trade office programs. These all remained fairly constant for the Department of Commerce, with federal revenues increasing while both transfers and program income decreased. Total revenues and other sources were \$21,541,946 for the year ended June 30, 2007 as compared to \$21,844,104 for the year ended June 30, 2006.

Federal revenues increased due to additional monies received for several grant programs. During fiscal year 2006, program income included \$700,000 received from the development fund and State Mill and Elevator Association pursuant to Senate Bill 2018, Section 28 and Senate Bill 2014, Section 19 of the 59<sup>th</sup> Legislative Assembly for the purpose of funding the International Business and Trade Office.

Total expenditures for the Department of Commerce were \$29,897,060 for the year ended June 30, 2007 as compared to \$30,136,082 for the prior year. The decrease in total expenditures for the audited period reflects a decrease in operating fees and services related to advertising expenses as well as in transfers given out. All other expenditures remained fairly constant.

## ***ANALYSIS OF SIGNIFICANT CHANGES IN OPERATIONS***

The Department of Commerce implemented a Local Economic Developer Certification program pursuant to Senate Bill 2018 Section 38 of the 59<sup>th</sup> Legislative Assembly and North Dakota Century Code (NDCC) 54-34.3-15. The educational services of the program are contracted to the National Development Council and participants that complete the program requirements receive professional certification.

Pursuant to Senate Bill 2018 Section 39 of the 59<sup>th</sup> Legislative Assembly and NDCC 54-44.5-09, the Department of Commerce established the Office of Renewable Energy and Efficiency to assist in the development of renewable energy within North Dakota to provide secure, diverse, sustainable, and competitive renewable energy supplies and promote the conservation of energy and the wise use of energy resources in both the public and private sectors.

The Department of Commerce has organized the Image Information program (KnewView) pursuant to Senate Bill 2018 Section 41 of the 59<sup>th</sup> Legislative Assembly and NDCC 54-60-12 for use by state agencies to assist state agencies and employees to present to the public a positive image of the state.

The Business Hotline program created pursuant to Senate Bill 2018 Section 42 of the 59<sup>th</sup> Legislative Assembly and NDCC 54-60-13 provides in-state and out-of-state callers with information regarding how to do business in the state, the services and assistance available to businesses, the advantages of doing business in the state, and information on state and other resources that provide assistance to businesses in the state.

## ***ANALYSIS OF SIGNIFICANT VARIANCES BETWEEN FINAL BUDGETED AND ACTUAL EXPENDITURES***

The amount of grant appropriations reflects the anticipated spending authority that was needed. The large unexpended appropriation amount occurred because anticipated grants from the federal government either didn't happen or weren't as much as anticipated.

# Financial Statements

## STATEMENT OF REVENUES AND EXPENDITURES

	June 30, 2007	June 30, 2006
<b><u>Revenues and Other Sources:</u></b>		
Federal Revenue	\$ 14,923,832	\$ 14,195,499
Loan Principle and Interest	1,696,222	1,721,257
Program Income	124,504	814,853
Development Fund	260,181	332,985
Interest and Investment Earnings	191,371	132,933
Sales and Services	54,099	80,836
License, Permits and Fees	38,778	19,350
Transfers In	4,252,959	4,546,391
<b>Total Revenues and Other Sources</b>	<b>\$ 21,541,946</b>	<b>\$ 21,844,104</b>
<b><u>Expenditures and Other Uses:</u></b>		
Grants, Benefits, and Claims	\$ 20,469,916	\$ 19,780,027
Salaries and Benefits	3,889,883	3,569,710
Operating Fees and Services	2,294,184	3,263,753
Fees – Professional Services	1,109,425	1,142,172
Printing	416,634	484,899
Travel	315,150	392,106
Rentals/Leases	240,188	266,727
Postage	225,835	144,491
Professional Development	207,258	226,995
Supplies	196,576	137,109
Equipment Under \$5,000	68,142	59,196
Equipment Over \$5,000	18,443	
Other Operating	186,345	203,385
Transfers Out	259,081	465,512
<b>Total Expenditures and Other Uses</b>	<b>\$ 29,897,060</b>	<b>\$ 30,136,082</b>

## STATEMENT OF APPROPRIATIONS

For The Biennium Ended June 30, 2007

<b>Expenditures by Line Item:</b>	<u>Original Appropriation</u>	<u>Adjustments</u>	<u>Final Appropriation</u>	<u>Expenditures</u>	<u>Unexpended Appropriation</u>
Salaries and Benefits	\$ 7,761,428		\$ 7,761,428	\$ 7,123,941	\$ 637,487
Operating Expenses	9,531,968		9,531,968	7,707,382	1,824,586
Capital Assets	25,000		25,000	18,443	6,557
Grants	50,102,870		50,102,870	34,867,968	15,234,902
Discretionary funds	1,450,127	\$ 652,102	2,102,229	1,471,689	630,540
Economic Development Initiatives	644,568		644,568	307,774	336,794
APUC	3,016,000	1,092,503	4,108,503	2,440,147	1,668,356
Lewis and Clark Bicentennial	3,933,103		3,933,103	3,871,204	61,899
Economic Development Grants	150,000		150,000	150,000	
<b>Totals</b>	<u>\$ 76,615,064</u>	<u>\$ 1,744,605</u>	<u>\$ 78,359,669</u>	<u>\$ 57,958,548</u>	<u>\$ 20,401,121</u>
<b>Expenditures by Source:</b>					
General Fund	\$ 19,180,781	\$ 1,026,120	\$ 20,206,901	\$ 18,408,436	\$ 1,798,464
Other Funds	57,434,283	718,485	58,152,768	39,550,112	18,602,657
<b>Totals</b>	<u>\$ 76,615,064</u>	<u>\$ 1,744,605</u>	<u>\$ 78,359,669</u>	<u>\$ 57,958,548</u>	<u>\$ 20,401,121</u>

### Appropriation Adjustments:

The \$1,092,503 increase in the APUC line includes carryover funds from the previous committed grants as stated in Senate Bill 2018 Section 17 of the 59<sup>th</sup> Legislative Assembly.

The \$652,102 increase in the Discretionary Grants line is carryover funds from the previously committed grants as stated in the Senate Bill 2018 Section 18 of the 59<sup>th</sup> Legislative Assembly.

### Expenditures Without Appropriations Of Specific Amounts:

Ethanol Production Incentive Fund has a continuing appropriation by NDCC 4-14.1-10 (\$1.35 million of expenditures for this biennium).



## *Internal Control*

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In our audit for the biennium ended June 30, 2007, we identified the following areas of the Department of Commerce's internal control as being the most important:

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### Internal Controls Subjected To Testing

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- Controls surrounding the processing of revenues.
- Controls surrounding the processing of expenditures.
- Controls effecting the safeguarding of assets.
- Controls relating to compliance with legislative intent.
- Controls surrounding the ConnectND (PeopleSoft) system.
- Controls surrounding the computer-based HOMENet.

We gained an understanding of internal control surrounding these areas and concluded as to the adequacy of their design. We also tested the operating effectiveness of those controls we considered significant. We concluded that internal control was not adequate, noting certain matters involving internal control and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgment, could adversely affect Department of Commerce's operations or ability to record, process, summarize, and report financial data consistent with the assertions of management in financial statements. Reportable conditions are described below. We also noted other matters involving internal control that we have reported to management of the Department of Commerce in a management letter dated August 21, 2007.

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### Finding 07-1

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#### **INVESTMENTS CONTROLS WEAKNESS**

The Department of Commerce has not been reconciling on a regular basis the bank balance of investments (approximately \$1.7 million) to the investment balance on ConnectND Financials. Subsequent to an accounting system conversion error, the Department of Commerce discontinued consistent reconciling procedures.

Good internal controls require an investment reconciliation of the bank balance to the book balance. Without this reconciliation, errors and irregularities would go undetected.

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### Audit Recommendation and Agency Response

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#### **Recommendation:**

We recommend the Department of Commerce reconcile the investment balance on ConnectND Financials to the Bank of North Dakota balance on a regular basis.

## Department of Commerce Response:

*The Department of Commerce temporarily halted reconciling the investment balance on Connect ND Financials to the Bank of North Dakota balance due to a discrepancy in the two reports. An error was made during the transfer of the funds from the SAMIS accounting system to the Peoplesoft accounting system. Once the State Treasurer's office made the correcting entry, the reports reconciled. Commerce will continue to reconcile these reports in the future.*

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### Finding 07-2

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## INVENTORY CONTROLS WEAKNESSES

The Department of Commerce maintains approximately \$30,000-\$40,000 in resale inventory related to ND Tourism. Adequate policies and segregated responsibilities have not been established to ensure proper controls surrounding re-sale inventory. Weaknesses noted are:

- Records of inventory sales and purchases are now maintained. However, if there are discrepancies between the inventory records and the actual quarterly inventory count, the electronic records are overwritten rather than adding documentation of adjusting entries to the electronic records.
- A bench mark has been established as a limit for merchandise that is given away for promotional purposes; however, a monitoring process is not in place to evaluate the reasonableness of the benchmark and the use of merchandise giveaways as a promotional tool.
- Segregation of duties does not exist between maintaining the inventory records, taking inventory, and making adjustments to the inventory records based on the actual inventory counts.
- Fluctuations for every inventory transaction including purchases, sales, and adjustments are manually calculated in the inventory records rather than establishing formulas within the spreadsheets to automatically calculate inventory balances.
- The quarterly inventory reconciliation and adjustments made to electronic records are not properly reviewed and approved.

Good internal control requires segregation of duties and that inventory be properly maintained, monitored, and tracked. Without proper controls, the Department may never know if inventory is lost, stolen, or given away inappropriately.

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Audit Recommendation and  
Agency Response

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**Recommendation:**

We recommend the Department of Commerce implement proper internal controls over inventory.

**Department of Commerce Response:**

*The Department of Commerce purchased an inventory software package that is addressing the control weaknesses regarding the inventory records. A process has been put in place to ensure that quarterly inventory reconciliation and adjustments are properly reviewed and approved. The budget for promotional gifts is being monitored and evaluated annually. The appropriate segregation of duties has been implemented.*

## *Compliance With Legislative Intent*

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In our audit for the biennium ended June 30, 2007, we identified and tested the Department of Commerce's compliance with legislative intent for the following areas that we determined to be significant and of higher risk of noncompliance:

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### *Legislative Intent Subjected To Testing*

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- Proper use of the State Treasurer (State Constitution, article X, section 12).
- Compliance with appropriations (2005 North Dakota Session Laws chapter 46).
- Compliance with procurement procedures (OMB Purchasing Procedures Manual, ND Administrative Code Chapter 4-12).
- Travel-related expenditures are made in accordance with OMB policy and state statute.
- Proper use of outside bank accounts, petty cash funds, and proper authority for investments outside the Bank of North Dakota.
- Adequate blanket bond coverage of employees (NDCC section 26.1-21-08).
- Compliance with fixed asset requirements including record keeping, surplus property, lease and financing arrangements in budget requests, and lease analysis requirements.
- Compliance with payroll related laws including statutory salaries for applicable elected and appointed positions, and certification of payroll.

The results of our tests disclosed one instance of noncompliance that is required to be reported under *Government Auditing Standards*. This finding is described below. Other than this finding, we concluded there was compliance with the legislative intent identified above.

### **NONCOMPLIANCE WITH PROCUREMENT LAWS**

The Department of Commerce does not have controls in place to properly ensure procurement procedures are performed in accordance with Dakota Century Code (NDCC), North Dakota Administrative Code (NDAC) Chapter 4-12, and North Dakota State Procurement Office Guidelines.

During testing procedures, several instances were noted where the Department of Commerce did not follow proper state procurement procedures and documentation for contracts under which payments were made during the audit period.

- NDAC Section 4-12-08-04, subsection 10, states that after proposals have been evaluated and a successful vendor selected, notice of intent to award must be promptly issued to all offerors that submitted proposals. Two instances were noted where the Department of Commerce did not issue a notice of intent to award letter.
- NDAC Section 4-12-11-02, states that preference given to North Dakota bidders must be equal to the preference given or required by the state of nonresident bidders, in accordance with NDCC 44-08-01. Two instances were noted where the Department of Commerce did not document indication of North Dakota bidder preference in evaluating and selecting vendors.
- NDAC Section 4-12-08-04 subsection 2 states that request for proposals must include all contractual terms and conditions as well as the relative importance of price and other factors or subfactors, if any. In addition, NDAC 4-12-11-01 states that a contract award will be made according to the evaluation criteria specified in the solicitation. Two instances were noted where the Department of Commerce issued request for proposals that had insufficient or no specified solicitation criteria. Subsequently, the evaluation criteria and relative weight of criteria factors did not correlate with the solicitation criteria.
- NDCC 54-44.4-09 requires vendors to be approved through the Office of Management of Budget and applicable vendors to register with the Secretary of State. Any waiver of the approval requirement must be stated in the solicitation. In addition, State Procurement Office Guidelines Chapter 6.3 indicates bidders should be required to provide proof of license, permit, or registration to perform business in North Dakota. The Department of Commerce did not state a waiver for the approval requirement and does not appear to require proof of licensure, permit, or registration and subsequently entered into contracts with two vendors that were not

approved with the Office of Management and Budget nor registered with the Secretary of State to perform business in North Dakota.

- NDCC 34-14-04.1 requires every employer to withhold from compensation due to employees those amounts which are required by state or federal law to be withheld. State Procurement Office Guidelines Chapter 5.13 outlines conditions that indicate an employer/employee relationship may exist. The Department of Commerce entered into a contract with a former employee where the employer/employee relationship conditions are evident by: providing a state government owned computer and email address; bidder's lack of authorized vendor registration with the Secretary of State indicating the individual is not in business to provide the same or similar services to other entities or the general public; unspecified scope of work including 'other duties as assigned'; and allowing the potential bidder to provide consultation as to the scope of work of the project.

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Audit Recommendation  
and Agency Response

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**Recommendation:**

We recommend the Department of Commerce:

- a) obtain adequate training of the state procurement procedures and requirements,
- b) implement adequate review procedures by an individual knowledgeable of the procurement process, and
- c) establish proper documentation to ensure compliance with North Dakota Administrative Code Chapter 4-12, NDCC 54-44.4-09 and State Procurement Office Guidelines.

**Department of Commerce Response:**

*The Department of Commerce clearly recognizes the importance of procurement regulations. In the Spring of 2007 our Procurement Officer received additional training and then implemented an in-house training session for all of Commerce staff. We will conduct these in-house training sessions on an annual basis. As a result of this recommendation Commerce reorganized duties internally and assigned a new staff person who has 8 years of state procurement experience with another agency to manage the procurement process. A detailed procurement policy specific to Commerce has been drafted and is currently being approved by senior staff and the state Procurement Office. Commerce will be in compliance with all procurement procedures in the future.*

## **ECONOMIC DEVELOPMENT GRANTS IMPROVEMENTS**

### **Point of Interest:**

The Department of Commerce administers economic development grants to public and private entities for the primary purpose of creating, expanding, or retaining businesses and jobs throughout the state. There is increasing public scrutiny of how tax dollars are being used to award economic development grants to businesses on the premise of creating jobs and economic growth to their community. Monitoring plans for economic development grants need to be properly structured and implemented to ensure funds are used as intended.

### **Challenge:**

Economic development grants provided through the Partners in Marketing discretionary grant, Community Development Block Grant (CDBG), and Centers of Excellence grant programs were selected in reviewing the Department of Commerce's policies and procedures compared to best practice guidelines. During the audit period, approximately \$27 million of federal and state funded grants and loans were provided through these programs to city and county governments, college and universities, and community development foundations.

The Department of Commerce is authorized to distribute Partners in Marketing discretionary grants pursuant to Senate Bill 2018, Section 27 of the 59<sup>th</sup> Legislative Assembly.

CDBG program grants are distributed within federal grant appropriation authority.

It should be noted that during our audit period, responsibility for performance monitoring of the Centers of Excellence grants did not reside with the Department of Commerce. We commend the Department of Commerce for recognizing that Centers of Excellence grants were not being monitored and working proactively to have legislation introduced to amend North Dakota Century Code Chapter 15-69 (effective August 1, 2007) authorizing the Centers of Excellence Commission to request the Department of Commerce to assist with pre-award reviews and post-award monitoring.

## **Improvements:**

Our review of the Department of Commerce's process and procedures for ensuring grant accountability and performance monitoring of economic development grants resulted in the following potential improvements:

### **Partners in Marketing Program Discretionary Grants**

- Documented performance monitoring of grant award guidelines need to ensure that award activity is carried out as intended, funds are spent appropriately, and the grant is achieving the desired results.
- Expenditures reimbursed through the grant award should be based on appropriate verified evidence to avoid improper payments and misuse or waste of funds.
- A final contract or agreement should be signed by both the grantor and grant recipient to ensure acknowledgment and acceptance of grant award terms.

### **CDBG**

- Post-completion inspection or reporting should be performed or required to ensure created jobs are retained for a reasonable period.

### **Centers of Excellence**

Recognizing that the responsibility for the Centers of Excellence program did not reside with the Department of Commerce during the audited period, the following best practices should be addressed by Commerce in implementing appropriate monitoring procedures:

- Application for funds should include a work plan indicating how the monies will be spent and in what timeframe.
- Assessments to support funding decisions should include appropriate investigation and be properly documented.
- Award agreements should include conflict of interest statements, information and reports the grantee is required to provide, results expected to be achieved and methods used to measure the results, and consequences for not achieving expected results.



- Policies and procedures should be prepared to include provisions for holding awarding organizations and grantees accountable for properly using funds and achieving agreed-upon results.
- Monitoring standards should be established and documented to ensure consistency in monitoring procedures.
- Site visit procedures should be developed to allow for consistent on-site monitoring, quantifying results, and performing comparisons over time and against preset standards.
- Performance monitoring evaluations should be documented to ensure award activity is carried out as intended, funds are spent appropriately, and the grant is achieving the desired results such as job creation.

**Criteria:**

The best practices used for our recommendations were selected from the following four publications: Guide to Opportunities for Improving Grant Accountability; Best Practice Guide for the Administration of Grants; Best Practices in Carrying Out State Economic Development Efforts; and Guide on Grants, Contributions, and Other Transfer Payments. These best practice studies were prepared by federal and state organizations including the Department of Treasury and Finance and the National State Auditor's Association to focus attention on the importance of grant accountability and provide sufficient best practice for establishing guidelines that will result in efficient, effective, and accountable grant administration and performance monitoring.

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Audit Recommendation  
and Agency Response

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**Recommendation:**

We recommend the Department of Commerce strengthen grant accountability administration and monitoring policies and procedures surrounding economic development grants.

***Department of Commerce Response:***

*The Department of Commerce has implemented all of the above recommendations regarding the Partners in Marketing Program. The Community Development Block Grant Program is funded through federal funds and therefore is excluded from the accountability legislation. Nevertheless, in implementing the accountability legislation in the 2005-07 biennium, Commerce*

*voluntarily applied the accountability legislation to the Community Development Block Grant Program when the funds are used for business development purposes. Therefore, the Community Development Block Grant Program will comply with the recommendation by virtue of compliance with the accountability legislation. As indicated, Commerce recognized early on the need for monitoring procedures for the Centers of Excellence program. Many of the above suggestions have already been implemented and Commerce is in the process of implementing the appropriate remaining procedures. Commerce is currently hiring an Accountability Officer to focus on this monitoring. Commerce intends to continue to work with the Auditors Office to research how the University System and/or university or college conflict of interest policies might apply to programs or projects funded through the Centers of Excellence program. The Centers of Excellence Commission's ability to enforce consequences is limited to withholding undistributed funds. Withholding of funds is an extreme event in which serious operational problems are identified that create unanticipated risk and compromise the state's investment in the Center.*

## ***Prior Recommendations Not Implemented***

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Prior recommendations have been implemented with the exception of the following:

### ***INVENTORY PROCEDURES – CONTROL WEAKNESSES***

#### **Background**

The Department of Commerce maintains resale inventory for the purpose of promoting North Dakota. Internal control procedures must be in place and operating effectively to safeguard assets.

#### **Recommendation**

Controls surrounding inventory for resale at the Department of Commerce are not adequate. Weaknesses noted are:

- An inventory is taken on a semi-annual basis and if there are discrepancies between the inventory records and the actual count, the records are changed with no documentation kept of the discrepancy or the adjustment made to the electronic records.
- Merchandise is given away for promotional reasons without a benchmark set as to how much should be given away.
- For every inventory transaction, the inventory count shown on the spreadsheet is changed by overwriting the number and no record exists of the actual activity; and
- Segregation of duties does not exist between keeping the inventory records, taking inventory, and making adjustments to the inventory records based on the actual inventory count.

#### **Status**

Partially implemented, see new recommendation on page 15.

## ***Management Letter (Informal Recommendations)***

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August 21, 2007

Mr. Shane Goettle, Commissioner  
Department of Commerce  
Century Center  
1600 E. Century Avenue – Suite 2  
Bismarck, North Dakota 58503

Dear Commissioner Goettle:

We have performed an audit of the Department of Commerce for the biennium ended June 30, 2007, and have issued a report thereon. As part of our audit, we gained an understanding of the Department of Commerce's internal control structure to the extent we considered necessary to achieve our audit objectives. We also performed tests of compliance as described in the same report.

Our audit procedures are designed primarily to enable us to report on our objectives including those related to internal control and compliance with laws and regulations and may not bring to light all weaknesses in systems and procedures or noncompliance with laws and regulations which may exist. We aim, however, to use our knowledge of your organization gained during our work to make comments and suggestions which we hope will be useful to you.

In connection with the audit, gaining an understanding of the internal control structure, and tests of compliance with laws and regulations referred to above, we noted certain conditions we did not consider reportable within the context of your audit report. These conditions relate to areas of general business practice or control issues that have no significant bearing on the administration of federal funds. We do, however, want to present our recommendations to you for your consideration and whatever follow-up action you consider appropriate. During the next audit we will determine if these recommendations have been implemented, and if not, we will reconsider their status as non-reportable conditions.

The following present our informal recommendations.

### **REVENUE**

We recommend that someone independent of draw downs reconcile the monies disbursed by the federal government (from a federal source) to the amount received from the federal government.

We recommend the Department of Commerce develop proper policies and procedures for credit card refunds including a procedure for proper documentation to be maintained and reviewed by an appropriate individual for unusual patterns or transactions. We also recommend all credit card refunds be approved by an appropriate individual.

## **FIXED ASSETS**

We recommend the Department of Commerce restrict access to fixed asset records to only necessary individuals and ensure segregation of duties surrounding fixed assets to ensure that individuals authorized to approve additions and deletions and perform year-end inventory are independent of individuals with access to the fixed asset records on ConnectND.

## **PAYROLL**

We recommend the Department of Commerce adequately review the coding of salaries to assure coding is accurate.

We recommend the Department of Commerce ensure segregation of duties between payroll data entry and approval responsibilities.

## **GENERAL**

We recommend the Department of Commerce properly restrict access to the ConnectND general ledger to ensure segregation of duties between data entry and approval responsibilities of correcting entries.

Management of the Department of Commerce agreed with these recommendations.

I encourage you to call myself or an audit manager at 328-2243 if you have any questions about the implementation of recommendations included in your audit report or this letter.

Sincerely,

Allison Bader  
Auditor in-charge